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Foreign Exchange Guarantees in China

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The rapid rise in China's external debt following the late-1984 decentralization of borrowing authority brought a retightening of controls by the People's Bank of China in late 1985. Included in the measures to regain control over foreign borrowing was a State Council directive that all foreign loans be preapproved by the State Administration for Exchange Control (SAEC), a department in the People's Bank of China. This recentralization also affected the issuing of guarantees for foreign borrowings, with all guarantees subject to SAEC approval. In addition, last February Beijing enacted stricter regulations on the issuance of guarantees (see appendix A).

While establishing its authority over the issuance of foreign exchange guarantees, Beijing in the last year has nearly doubled the number of institutions authorized to grant guarantees. According to a recent issue of the Hong Kong-based Ming Pao, 82 institutions can now provide foreign exchange guarantees (see appendix B). These include the

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country's major banks, foreign banks with branches in China, the China International Trust and Investment Corporation (CITIC), and various municipal and provincial international trust and investment corporations. In addition, any Chinese institution with foreign exchange income can apply to the SAEC for permission to issue a foreign exchange guarantee on a case-by-case basis.

In an effort to minimize the inherent risks in guaranteeing project financing, the stricter regulations obligate the guarantor to thoroughly investigate the feasibility of the project to be guaranteed, check on the creditworthiness of the debtor, and plan measures in advance should the guarantee be called upon. Similar guidelines are expected in the coming months with regard to overseas borrowing for projects. The tightened controls on foreign exchange guarantees parallel Beijing's policy that those who borrow overseas--and their guarantors--should bear full responsibility for loan repayments; Beijing will not act as the ultimate guarantor. In most instances where loan repayments could not be met, foreign borrowers have been bailed out by their guarantors or investment partners. Earlier this year, when a number of troubled loans made news and caused considerable concern among foreign banks, high-level provincial officials stepped in and took responsibility for the commitments.



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Appendix A

Provisional Regulations on the Control of Foreign Exchange Guarantees Provided by Institutions on Chinese Territory

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1. The regulations are formulated in order to promote economic and technical cooperation with foreign countries, ensure smooth development of financial activities, and strengthen control over foreign exchange guarantees.
2. The foreign exchange guarantees mentioned in the regulations are guarantees provided by guarantors to creditors for paying off debts with their own foreign exchange when a debtor is unable to meet his obligation of paying off a debt in accordance with a contract.
3. The departments that control foreign exchange guarantees are the State Administration of Exchange Control and its branches (hereafter referred to as "foreign exchange control departments."
4. Institutions entitled to provide foreign exchange guarantees to debtors include:
 - a. Authorized Chinese financial institutions engaged in foreign exchange guarantee services.
 - b. Nonfinancial enterprises with legal person status and with foreign exchange income.

The total amount of foreign exchange guarantees provided by any financial institution and the total amount of its debts together must not exceed an amount equal to 20 times its own funds in foreign exchange. The total amount of foreign exchange guarantees provided by any nonfinancial institution must not exceed an amount equal to its own funds in foreign exchange.

5. Foreign exchange guarantees can be made within the following scope:
 - a. Guarantees can be provided to enterprises in China that are registered according to Chinese law, but no guarantee can be issued for the enterprise's registered capital.
 - b. Without the permission of China's foreign exchange control departments, no guarantee can be provided for Chinese enterprises stationed overseas.

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c. No guarantee can be provided for China-based foreign institutions and foreign-invested enterprises unless they have the same value in foreign exchange assets as mortgage for the guarantee.

6. Before providing any guarantee, the guarantor must do the following work:

a. Analyze and study the feasibility of the project for which it will provide the guarantee.

b. Fully understand the debtor's creditworthiness.

c. Adopt necessary countermeasures to guard against any eventualities with regard to the guarantee provided.

7. In providing foreign exchange guarantees, the guarantor must sign a written contract clearly stipulating the rights and obligations of the guarantor, the creditor, and the debtor.

8. A creditor has the right to demand that the guarantor provide him with the relevant information such as a financial report and information on foreign exchange earnings and expenditures.

9. After a guarantor provides a guarantee, the debtor and the creditor must obtain the guarantor's concurrence if they need to revise the contract under guarantee. The guarantor will be automatically relieved from its obligation for the contract if the original contract is revised without the guarantor's concurrence.

10. After a guarantor provides a guarantee, he should fulfill his obligation if the debtor fails to discharge his obligation as specified in the contract under guarantee as long as the contract is still valid. After fulfilling his obligation in providing the guarantee, the guarantor has the right to demand that the debtor pay him compensation for his losses.

11. After providing its guarantee, if the creditor does not fulfill his contractual obligations during the term of the guarantee, the guarantor will be automatically released from his obligations. The guarantor has the right to ask the creditor to compensate for its losses accordingly.

12. The guarantor, after providing his guarantee, has the right to oversee the debtor's funds and financial affairs. The guarantor and debtor may negotiate and define specific ways to oversee.

13. In light of the actual risks of the guarantee, the guarantor has the right to ask the debtor to provide mortgage in kind and to collect a fixed amount of guarantee fee.

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14. Within 10 days after providing a guarantee, the institution in China shall submit a guarantee contract and related materials to local foreign exchange administration departments for the record.
15. Foreign exchange administration departments will warn, fine, or revoke the right to provide foreign exchange guarantee service from those institutions and units that violate these regulations according to the seriousness of the case.
16. The right of interpreting these regulations belongs to the State Administration of Exchange Control.
17. These regulations will go into effect from the date of promulgation.



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Appendix B

China's Foreign Exchange Guarantors*

Bank of China and its branches
Shanghai Branch of the Hongkong and Shanghai Banking Corp.
Shanghai Branch of Standard Chartered Bank
Shanghai Branch of Overseas Chinese Banking Corp. Ltd.
Shanghai Branch of the Bank of East Asia Ltd.
Shenzhen Branch of Nanyang Commercial Bank
Shekou Branch of Nanyang Commercial Bank
Zhuhai Branch of Nantong Bank
Shenzhen Branch of Guangdong Provincial Bank
Investment Bank of China
Xiamen International Bank
Shenzhen Branch of the Hongkong and Shanghai Banking Corp.
Bank of Credit and Commerce International (Overseas) Limited
Xiamen Branch of United Overseas Bank
Shenzhen Branch of Banque Indosuez
Shenzhen Branch of Standard Chartered Bank
Xiamen Branch of Chiyu Banking Corp. Ltd.
Shenzhen Branch of Societe Generale
Xiamen Branch of the Hongkong and Shanghai Banking Corp.
Xiamen Branch of Bank of the Orient
Shenzhen Branch of Banque Nationale De Paris
Shenzhen Branch of the Hokkaido Takushoku Bank Ltd.
Shenzhen Branch of the Sanwa Bank Limited
China International Trust and Investment Corp.
Shanghai Investment & Trust Corp.
Guangdong International Trust & Investment Corp.
Fujian Investment Trust & Enterprise Corp.
Hubei International Trust & Investment Corp.
Tianjin International Trust & Investment Corp.
Zhejiang International Trust & Investment Corp.
Bank of China Trust & Consultancy Co.
Liaoning International Trust & Investment Corp.
Jiangsu International Trust & Investment Corp.
Beijing International Trust & Investment Corp.
Jiangxi International Trust & Investment Corp.
Shenzhen International Trust & Investment Corp.
Shenyang International Trust & Investment Corp.
Chongqing International Trust & Investment Corp.
Shanxi Joint Financial Investment Corp.
Shenzhen Branch of Guangdong International Trust & Investment Corp.
Commercial Bank of China Trust & Investment Corp.
Zhongyuan Development Trust & Investment General Corp.
Sichuan Changjiang International Trust & Investment Corp.
Anhui International Trust & Investment Corp.

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Jilin International Trust & Investment Corp.
Ningxia Islam International Trust & Investment Corp.
Shantou International Trust & Investment Corp.
Henan International Trust & Investment Corp.
Shanxi Economic Development & Investment Corp.
Guangxi International Trust & Investment Corp.
Hunan International Trust & Investment Corp.
China Venturetech Investment Corp.
Dalian International Trust & Investment Corp.
Nanjing International Trust & Investment Corp.
Faoshan Branch of the Industrial and Commercial Bank of China
Shantou Branch of the Industrial and Commercial Bank of China
Fuzhou Branch of the Industrial and Commercial Bank of China
Guangzhou Branch of the Agricultural Bank of China
Ningbo International Trust & Investment Corp.
Wuhan International Trust & Investment Corp.
Guangzhou (EDZ) International Trust & Investment Corp.
Faoshan International Trust & Investment Corp.
Xinjiang International Trust & Investment Corp.

*This list is compiled from various press sources and should not be considered comprehensive.



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